

Rev. Rul. 61-87, 1961-1 C.B. 191, amplified Rev. Rul. 63-220

A corporation primarily formed for the purpose of making unsecured loans to students at low rates of interest for completing their educational programs and guaranteeing for a fee the repayment of such loans when made to qualified students by commercial banks is exempt from Federal income tax under section 501(a) of the Internal Revenue Code of 1954 as an organization described in section 501(c)(3) of the Code, if it is shown to be organized and operated exclusively for charitable and educational purposes.

Advice has been requested whether a corporation, which is organized for and engaged in making loans to students for educational purposes, loans to educational institutions for supplementing their student loan funds and guaranteeing the repayment of a specified percentage of the principal amount of loans made to students for educational purposes by commercial banks, may qualify for exemption from Federal income tax under section 501(a) of the Internal Revenue Code of 1954 as a charitable and educational organization described in section 501(c)(3) of the Code.

The instant corporation was chartered by a special act of a state legislature for the purpose of helping qualified students who are domiciled in the state to obtain funds otherwise unobtainable with which to complete their educational programs. The articles of incorporation provide that in carrying out its purposes the corporation shall always be operated exclusively for charitable and educational purposes and that no part of its earnings shall ever inure to the benefit of any shareholder or member of the corporation. It is also provided that in the case of dissolution the assets of the corporation shall be distributed for a public charitable purpose.

The corporation is authorized by its charter to make loans directly to students or their parents or guardians for educational purposes, to make loans to educational institutions for supplementing their student loan funds and to guarantee approved loans made by commercial banks to qualified students for educational purposes. The corporation maintains a reserve fund of ten percent of its outstanding guaranteed loans with which to meet its obligations in this regard. The student loans are made at comparatively low rates of interest. In the case of guaranteed loans, the lending institution pays the corporation a small fee for its guarantee. Loans to approved educational institutions are likewise made at low rates of interest.

To be eligible for a loan, a student must, among other things, be enrolled in an approved educational institution and must have satisfactorily completed the first academic year of his educational program. Loans are limited to \$500 during any one academic year, with an overall limitation of \$1,500. These loans are made on an unsecured basis and for terms up to six years.

The corporation's income is derived from contributions, fees for guaranteed loans and interest on investments. Disbursements are made for loans, for the cost of advertising to acquaint students and institutions with the corporation's student loan program, and for operating expenses.

Section 501(c) of the Code describes certain organizations which are exempt from income tax under section 501(a) of the Code and reads, in part, as follows:

(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, \* \* \* or educational purposes, \* \* \* no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, \* \* \*.

In order to qualify for exemption under the above-cited provisions of law, an organization must be both organized and operated exclusively for one or more of the purposes specified therein.

The question presented here is whether the making of loans under the circumstances stated constitutes a business of a kind ordinarily carried on for profit.

Students usually are not employed, and are not considered good credit risks. Commercial enterprises do not ordinarily make unsecured loans to students or guarantee their unsecured notes. Hence, students without substantial collateral usually find it extremely difficult to obtain loans through regular commercial channels to help finance their education.

The basic purpose of the instant organization, therefore, is to aid students in attaining an education. Such a purpose is regarded as charitable. The mere fact that interest is charged or that a fee is received for guaranteeing a loan is not sufficient, of itself, to deny exemption. Colleges exempt under section 501(c)(3) of the Code charge tuition. Moreover, organizations similarly organized and operated to make loans to students to assist them in obtaining their education are generally regarded as charitable organizations, though they charge interest.

Accordingly, it is held that the corporation is exempt from Federal income tax under section 501(a) of the Code as an organization described in section 501(c)(3), since it has been shown that it is organized and operated exclusively for charitable and educational purposes.

An organization may not consider itself exempt from tax merely because it falls within the scope of this Revenue Ruling. In order to establish its status, an organization claiming

exemption under section 501(c)(3) of the Code should file its application on Form 1023, Exemption Application, with the District Director of Internal Revenue for the internal revenue district in which is located the principal office of the organization. See section 1.501(a)-1 of the Income Tax Regulations. See also Rev. Rul. 54-164, C.B. 1954-1, 88.